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Beetsma, Roel; Gradus, Raymond

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Roel Beetsma and *Raymond Gradus*

Restarting the Dutch Economy after the Covid-19 Crisis*

As was the case for most other economies in the eurozone, the Dutch economy was severely hit by the corona crisis. Yet, it is also clear that, likely due to its high degree of digitalization and the nature of its knowledge-intensive economic activities, the setback was substantially smaller than for some other economies with a sectoral structure more focused on direct interpersonal interaction, such as tourism. Also, the rather flexible labor market has been conducive in mitigating the economic downfall. Even in the midst of the crisis, unemployment hardly increased compared with the 2019 level, while there was still substantial turnover in the job market. Adding to this the massive government support, the shrinkage of the economy was in fact smaller than at the height of the global financial crisis in 2009. According to CPB (2021b), the decline of GDP in 2020 would have been 0.6 percentage point larger and unemployment would have been 65–180 thousand employees higher had no business support been given.

Now that, following a reasonably successful vaccination campaign,[1] the corona crisis seems to be drawing to an end, the following question arises: what should the government do next in terms of economic and financial policies? The background situation is one of an economic outlook improving faster than anticipated and an increasing labor shortage in many sectors, which can be explained partly by the aging of the population and partly by a mismatch between the skills of those leaving school or the university and what is demanded by employers. The number of vacancies has risen above unemployment, which is now close to its (low) pre-corona level. Employment in hours is not yet back at its original level due to labor market withdrawals, but is expected to increase fast if the economy stays on its current trajectory. The current juncture is one of substantial uncertainty: while longer-run demand for labor will outpace its supply, a wave of bankruptcies in the aftermath of corona could temporarily alleviate labor market tightness and push employers into a wait-and-see mode. Indeed, the government has announced to wind down the general business support arrangements and will only continue to support specific sectors, such as the event industry and the tourism sector. For example, the government announced that the borrowing facility for traveling agencies will continue until the end of 2021.

Besides the aging and increasing labor shortages, the other major long-term challenge of current and future governments will be to handle the consequences of climate change and the transition from fossil to green energy. Both will require very substantial public and private sector investments. Notably, in this year's Budget Memorandum (2021), the government announced that it will invest an additional sum of over €6.8 billion in climate measures on top of the existing planned spending on climate policy in the coming years. In the following, we set out what are in our view the policy priorities after the corona crisis.

THE SUPPORT MEASURES

Most support during the corona crisis has gone to businesses, mainly through generic measures, but also through support of a number of major individual firms.[2] Support was initially conditional on not laying off employees. Later on, this condition was slightly relaxed. The rationale for the support was to prevent a sharp increase in unemployment and widespread business failure which, in turn, would further push up unemployment. Measured against these objectives the support policy was successful. Unemployment stayed below 4 percent in 2020, while the number of bankruptcies in 2020 is lower even than during the period before 2020 (Rabobank 2021).

The main measures on the expenditure side were a wage-cost compensation for firms with revenue losses (NOW), a compensation

* All remaining errors are our sole responsibility.

[1] End of August 2021 of those of 18 years or older 85 percent had received at least one vaccination, while more than 75 percent were fully vaccinated.

[2] A detailed discussion of the various support measures is contained in Beetsma and Gradus (2021).

Roel Beetsma

is Professor of Macroeconomics at the University of Amsterdam, Visiting Professor at Copenhagen Business School, and Member of the European Fiscal Board. He is also a fellow of CEPR, CESifo, Netspar, and the Tinbergen Institute.

Raymond Gradus

is Professor of Public Economics and Administration at the Vrije Universiteit Amsterdam. He is also a fellow of the Tinbergen Institute, Netspar, and chairman of the Committees for Financial Supervision of the Dutch Antilles.

for fixed costs (TVL), and temporary financial support for self-employed persons (TOZO). Each time package has been extended in principle by three months, while conditions have gradually become more favorable.[3] For example, while TVL was initially a fixed amount of 4,000 euros and later on the maximum was 1.2 million. These generic support measures have expired end of September 2021, after which only specific sectors such as the event industry continue to be supported. Measures have also been taken on the revenue side, mainly by allowing companies to postpone payment of corporate taxes.

The current estimates of the aggregate discretionary support are 35.4 billion euros in 2020 and 29.9 billion euros in 2021.[4] In addition, the government has provided 50.3 and 41.6 billion in terms of guarantees in 2020, respectively 2021, of which more than half is for Next Generation EU (NextGenEU). Next to the generic support, some firms have also received individual support. The largest beneficiary was airline KLM, which received a 90 percent guarantee on a 2.4 billion loan from private creditors (part of the aforementioned total amount of guarantees), a junior loan of 1 billion from the government, and direct wage support of more than 1.2 billion euros (part of NOW).

THE ECONOMIC OUTLOOK

At the moment of writing (September 2021), the Dutch economy is recovering quickly. Table 1, taken from Beetsma and Gradus (2021), provides the most recent macroeconomic projections from the Netherlands Bureau of Economic Policy Analysis (CPB 2021a). Projected GDP growth is well above 3 percent in both 2021 and 2022. In 2020, unemployment increased by an unusually small amount for a recession (although part of the labor force withdrew from the labor market), while it is expected to fall again in 2021 and to marginally increase in 2022. After a drop in 2020, employment is expected to grow in 2021 and 2022. The public finances look healthy, with public debt peaking at less than 58 percent of GDP in 2021. The public deficit deteriorated by almost 6 percentage points between 2019 and 2020 to 4.2 percent of GDP and is set to rise further to 5.4 percent in 2021, after which it is expected to fall back to 2.3 percent in 2022 when most of the discretionary support measures have expired. Hence, the deficit is well below the ceiling of the Stability and Growth Pact when the severe economic downturn clause is expected to be de-activated (as of the start of 2023). Inflation is projected to be close to 2 percent in both 2021 and 2022, despite the pickup of economic growth and the fall in the individual saving share of disposable income.

[3] In 2020, the second tranche was from 1 June till 30 September (Beetsma and Gradus 2021).
[4] The term “discretionary” is used to distinguish this support from the working of the automatic stabilizers.

POLICY PRIORITIES

Now that corona lockdowns seem to be coming to an end, what should be the economic-financial priorities for the Dutch government to restore from the economic devastation and make the economy fit for the long term?

Shorter-run Priorities

The priorities should address both the shorter and the longer run. The cabinet took the right decision to withdraw the generic business support by 1 October 2021. Support will only be continued for specific sectors that are still hurt by corona restrictions. Indeed, there no longer is any macroeconomic rationale for generic support. The potential usefulness of any continued support would be at the microeconomic level, in terms of alleviating the personal misery of small business owners. However, for this there would be other instruments, such as subsistence support for those who need it, that do not (or to a lesser extent) distort the allocations of labor and capital of the business sector. After all, the longer the support lasts, the more firms will adjust their behavior accordingly, for example by raising their share of debt financing in the expectation that the government will come to the rescue when they become unable to service the debt (Boot 2021). Further, keeping weak firms afloat hampers the reallocation of production factors towards those firms where they can be put to the best use.[5] This argument is of particular relevance in a labor market with an increasing shortage of qualified workers. Individuals who lose their job in a badly performing firm will easily find a new job in which they are more productive. Finally, the longer support lasts, the more opportunities firms find to abuse the support.

While the government’s quick response to corona has helped to stem the damage to the economy, be-

[5] Interestingly, there is clear evidence that weaker firms have made more use of the corona support than stronger firms. For a large sample of Dutch firms, Roelandt et al. (2021) demonstrated that firms that were less productive and less liquid before the crisis were more likely to make use of support.

Table 1

Realizations and Projections for the Dutch Economy, in %

Year	2019	2020	2021	2022
Real GDP growth	2.0	– 3.8	3.9	3.5
Unemployment level	3.4	3.8	3.4	3.5
Employment change (hours)	2.1	– 2.7	2.3	1.8
Inflation (HICP)	2.7	1.1	1.9	1.8
Budget balance (GDP)	1.7	– 4.2	– 5.4	– 2.3
Debt level (GDP)	48.5	54.3	57.5	56.5
Individual saving (disposable income)	4.5	11.6	11.4	6.8

Source: This table is taken from Beetsma and Gradus (2021). Figures in the table are based on CPB (2021a, August).

cause of the urgency the eligibility conditions were light and so were the checks on whether firms fulfilled these conditions. Based on the tax office's turnover figures in 2019 and 2020, Schellekens et al. (2021) suggest that a substantial part of the business support was eventually unjustified,[6] because a large fraction of the firms overestimated their sales losses. This was the case for an estimated 86 percent of the firms that applied for NOW 1.0 and 79 percent of the firms that applied for NOW 2.0. The average overestimation of the revenue loss was 32 percent, while the estimated excess pay-out was 33 percent for NOW 1.0 and 37 percent for NOW 2.0, or 4.2 billion euros in total. Moreover, more than 50 percent of the firms that applied for postponement of their tax payments experienced only a limited revenue reduction or even saw their revenues increase. Both for budgetary reasons and out of fairness to the taxpayers, it will be important to claim back any of the excess support given to firms.

A related matter that will land on the policymakers' desks is how to deal with the tax liabilities built up by firms during corona. To alleviate the financial pressure on firms the government has extended the maximum term to pay taxes to 60 months. There has been discussion about forgiving (part of the) tax obligations. So far, the government has refrained from the cancellation of tax obligations. No doubt, however, once tax arrears start threatening business continuity, pressure to forgive tax obligations will increase. However, this would come at the expense of taxpayers and blunt the competitive edge of well-functioning firms that do not benefit to the same extent from forgiveness. Finally, canceling tax obligations would only alleviate indebtedness of the business sector towards the government, if other creditors do not come forward too. It would in fact be a subsidy to these other creditors, mainly banks, because they can recover a larger fraction of their own claims.

The Netherlands is one of the two countries so far not to have submitted a recovery plan in the context of NextGenEU.[7] The current, outgoing government considers this the task of a new government. The recovery plan would require the government to specify reform measures (in areas identified earlier by the European Commission) and invest in digitalization and climate. On the one hand, there may be a reluctance in binding the next government to reforms that it may not embrace. On the other hand, however, EU funding of investment would be more than welcome, as the climate transition requires huge investments in the coming decades, such as investments in the upgrading of the capacity of the electricity grid, which will be needed to distribute the increase in green electricity, and investments in a hydrogen infrastructure. These investments will take time to implement. Hence, the sooner these investments are started, the better. Therefore, the government (outgoing or incoming) would be advised to no longer wait and start drawing up a recovery plan. It is important to realize that the investment proposed under the recovery plan can only be a small part of the full investment agenda that we discuss below.

Long-run Challenges

The Dutch government faces a number of long-term challenges. The most important ones are dealing with an increasing shortage of labor, financing and implementing the climate transition, and the position of the Netherlands in the EU.

The Increasing Shortage of Labor

The Dutch labor market was tight before the Covid-19 crisis and now tightness is almost back at its pre-corona level. Tightness can be expected to increase further with the aging of the population. Shortages in the technical sectors are particularly large, but now they are emerging in many other sectors as well. What should be done? The government needs to develop an integral vision on how to meet long-run labor shortages.

First, invest more and better in education at all levels. While our economy is becoming increasingly knowledge-intensive, school achievements by pupils, in particular reading and calculus, are on a declining trend. This phenomenon was already present before corona struck. However, corona has given this trend an extra push. At the same time there are increasing shortages of teachers, and these shortages are largest in poor "problem" neighborhoods. While teacher jobs are increasingly complicated, with parents becoming more assertive and teachers effectively having to take more care over the children, pay is lagging market wages. Education of good teachers, with commensurate pay and differentiation in pay for those subjects that are in the highest demand, will be essential. Focus should be on improving "hard" skills of pupils and avoiding drop-out from schools. Pupils that have dropped out from schools should be targeted to resume their studies, for example by providing guarantees for an internship. "Inclusiveness of education" is becoming a buzzword in the public debate. The step described here would benefit in particular youth from weaker socio-economic backgrounds, often from minority groups. The government should also raise investment in "hardware." Many school buildings are dilapidated with unhealthy conditions inside, thus not contributing to the achievements of pupils.

While labor market participation has been on a rising trend since the turn of the century, with a sub-

[6] It is important to note that this finding does not necessarily point to firms intentionally trying to claim more than they have a right to. The overestimation of their losses is probably mostly driven by the severe uncertainty. Moreover, a "general-equilibrium" effect may also play a role: the "excessive" support may have dampened the economic setback to such a degree that in the end it obviated a substantial fraction of support at the individual firm level.

[7] The other country is Bulgaria.

stantial fraction of the increase taking place through part-time work, there are still large groups not actively participating in the labor market, in particular people with a migration background. Many of those who are not participating failed to make it through school and are living on social assistance and some benefits. Politically, the easiest solution is to just leave them alone. However, the economy and society would benefit if those along the sidelines are stimulated into entering the labor market, if needed after appropriate schooling. This requires a policy of active stimulation. Individuals would need to be actively targeted and be offered training, possibly with some guarantee of internship or a temporary initial job. These carrots would also need to be accompanied by financial incentives. Marginal tax rates are relatively high in the Netherlands,[8] while the loss of benefits and various other forms of support makes it financially unattractive to trade the status of receiver of benefits for that of employee.

At the tertiary education level, the number of students in higher education has gone up dramatically, while public spending has not kept up, leading to large teacher-student ratios, thus putting pressure on the quality of the student turnout and raising work pressure on teachers. At the same time, "soft" studies such as festival management, leisure time studies, and the like, have become enormously popular. There are no incentives, other than those directly coming from the labor market, imposed on institutions of higher education to steer the relative sizes of their programs towards where the shortages are in the labor market. The game is to attract as many students as possible into programs that are relatively cheap to teach, thereby securing the financial viability of the department responsible for the teaching. Young people have a hard time to see through this. The macro-result is a mismatch between what the labor market demands and skills and knowledge of the supply on the labor market. New labor market entrants are disillusioned and end up in areas they have not studied for (so at a lower wage than needed) or they need retraining. Where the market fails more steering from above will be needed.

More investment in education will not be sufficient to eliminate future labor shortages. Life expectancy continues to rise and to finance these higher pension and healthcare costs people need to work longer. This is indeed happening. The number of people above 60 years who still work, full-time or part-time, has increased enormously since the turn of the century, partly because the official retirement age (for a public pension) has gone up and because elderly workers are in a better shape than before. Importantly, for the future there is also an automatic link between the (potential) increase of life-expectancy and age for the public pension. This makes it worthwhile for employers to invest through on-the-job training and courses in the skills of workers who are over 50 years, and it makes it worthwhile for the employees themselves to beef up their earnings capacity and remain attractive for the labor market.

A final source of labor would be immigration. Immigration of unskilled labor, often economic refugees, is unlikely to contribute significantly to solving labor market tensions. Language barriers and cultural differences make absorption in the workforce difficult. Unemployment of people coming from Morocco and the Antilles is three times higher than average and for Turkish people it is 2.5 times higher. Immigration of skilled labor does contribute to reducing shortages in areas of high demand. This is what is already happening. There is a substantial net inflow of foreign students, a fraction of which start their working career in the Netherlands. Companies in technical sectors "import" high-skilled foreigners on a large scale. Unfortunately, the number of years during which they receive a tax advantage has been reduced.[9]

Climate Policy

The Dutch government has spent billions in subsidies to stimulate driving electrically and for the production of renewable energy. The cost of reducing emissions per tonne CO_2 has been extremely high.[10] Fortunately, the aforementioned subsidies are being built down. There are better ways to spend public resources on dealing with climate change. Indeed, an enormous investment agenda lies ahead, both in terms of the energy transition and in terms of protectionary measures against natural disasters resulting from climate change. The latter would aim at dealing better with extreme weather in the form of droughts, flood from the rivers entering the country, and the rising sea level.

The energy transition requires a long-term investment agenda in which the private and public sector collaborate. Such long-term agenda is needed to provide the security needed to involve private parties, who have been complaining about the government changing its policies all the time. The main investments concern setting up parks that produce wind and solar energy and infrastructure investment, in particular increasing the capacity of the electricity grid (to enable the transportation of green electricity) and in the infrastructure for the transportation of hydrogen to be used mainly by the energy-intensive industry. It is important to realize that, along with the cost of financing these investments, there will also be a benefit in terms of innovation that increases the

[8] The highest marginal income tax rate of 49.5 percent sets in at a relatively low level of income.

[9] This is the so-called "30 percent rule": essentially income taxes are levied on 70 percent of gross income.

[10] According to a study by Dutch court of audit the cost of reducing emissions per tonne CO_2 by electronic cars was in 2018 approximately 1,700 euros. Gradus et al. (2017) shows a saving of 1 tonne of CO_2 through plastic recycling costs 180 euros in the Netherlands—also far higher than alternatives for saving CO_2, such as wind energy (€30).

efficiency of the transition and that may produce new export opportunities.

While with falling costs, investments in solar and wind energy production currently earn themselves back, the role of the government in bringing about the necessary infrastructure investments will be crucial. First, the government would need to initiate major infrastructure investments and coordinate these projects with the various private parties involved. Second, the government may need to provide co-financing or guarantees to the private parties involved. Beetsma et al. (2021) propose to set up a public-private investment bank designed specifically for the financing of these infrastructure projects. New public resources would not be needed, because the bank would replace the so-called Invest-NL and National Growth Fund, which are funded by the government to (help) finance growth-promoting investments. The bank would hold a long-term view with regard to its investments and not be subject to daily pressures from financial markets. This would also facilitate long-term commitments by the government. It would also draw in the right type of investors, which includes pension funds and insurance companies since they have long-term liabilities. However, other financiers with a long-term perspective would also be welcome. The presence of private sector parties is crucial, though. On the one hand, they provide part of the financing and share in the revenues and risks. On the other hand, they encourage a business approach, in which investment projects will be evaluated in the same way as regular commercial investment projects are evaluated for selection.

Stance on the EU

Unlike some other countries, and despite the importance of the EU internal market for the Netherlands, the Dutch political establishment does not seem to have a clear position as to the direction in which they would like to see the EU to develop and what should be the Dutch position in the EU. The consequences can be damaging. For example, mainstream politics is critical of new arrangements involving transfers to other parts of the EU but does not form a view on how they should be designed if the Netherlands is confronted with such plans by the Commission or other countries. This was the case with NextGenEU, which was backed by Germany, the most important partner country. Not participating was not an option, while the room for having its design amended was very limited. The report by the European Economy Expert Group (2021) describes four possible "integration preferences" (on the side of the Dutch government) with consistent policy packages leading towards a stable and resilient European economy. These preferences differ in terms of speed (gradual or accelerated), uniformity (all Member States simultaneously, or multi-speed), and the main mechanism (policy coordination or market discipline). Besides this, it will be important for Dutch politics to realize that the Netherlands is a geo-political dwarf and that, if it has the ambition to exert any influence in the world arena, this should be done as part of the EU as a bloc.

CONCLUDING REMARKS

Now that the corona-pandemic is largely behind us and the Dutch economy is recovering quickly, its government needs to return to its long-run policy priorities. This would require a long-term strategy in terms of how to secure a sufficient supply of qualified labor to keep the economy going and a plan on the appropriate investments in the energy transition and in dealing with the consequences of climate change, and how to finance these investments. Besides these, the government needs to develop a view on how it would like to see EU develop and what would be the place of the Netherlands in the EU.

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